



APPROVED MINUTES
APPROVED 08-22-11

CITY OF SCOTTSDALE
AUDIT COMMITTEE

MONDAY, June 20, 2011

CITY HALL
KIVA CONFERENCE ROOM
3939 NORTH DRINKWATER BOULEVARD
SCOTTSDALE, AZ 85251

REGULAR MEETING

PRESENT: Councilwoman Suzanne Klapp, Chair
Councilwoman Linda Milhaven

ABSENT: Vice-Mayor Robert Littlefield

STAFF: Kyla Anderson, City Auditor's Office
Joyce Gilbride, City Auditor's Office
Joanna Munar, City Auditor's Office
Sharron Walker, City Auditor's Office
Michelle Albanese, Community Services
Bill Murphy, Community Services
Jeff Nichols, Finance & Accounting
Ken Nemec, Human Resources

GUESTS: Carter Smitherman, LarsonAllen
Karen Lyzinski, LarsonAllen

CALL TO ORDER

Chair Klapp called the meeting to order at 4:00 p.m., noting that Vice Mayor Littlefield is traveling and will not be present.

1. Approval of Minutes, Regular Meeting, April 18, 2011

COMMITTEE MEMBER MILHAVEN MOVED TO APPROVE THE MINUTES OF THE APRIL 18, 2011 REGULAR MEETING. CHAIR KLAPP SECONDED THE MOTION, WHICH CARRIED BY A VOTE OF TWO (2) TO ZERO (0). COMMITTEE MEMBER LITTLEFIELD WAS ABSENT.

2. Discussion with Larson Allen LLP representative regarding the scope and timing of the City's Financial and Compliance Audit for FY 2011

Mr. Carter Smitherman of LarsonAllen said the preliminary external audit work was done in the last two weeks of May. The financial audit of the Community Facility Districts, the Scottsdale Preserve Authority and the Municipal Property Corporation will be done in the last week of August. A final audit of the balance sheet and revenues/expenses of the City will be performed from mid-September through early October. They plan to issue their audit reports by the end of October, to be followed by an exit conference with the Audit Committee.

Mr. Smitherman said that the preliminary audit work did not reveal any additional audit risks beyond areas which are inherent risks in every organization. They have held discussions with management and the City Auditor. They are not aware of any possible fraud. However, he added that if the Audit Committee members are aware of any suspicions of fraud, they will amend the audit plan. Neither Committee Member was aware of any such activity. He asked that if they should become aware of anything which the external auditors should investigate, that they bring it to their attention.

Mr. Smitherman said if their audit reveals any fraud, they address it immediately with the appropriate level of management and would bring it to the Committee's attention via the City Auditor. He stressed his willingness to answer their questions at any time.

3. Discussion and possible direction to staff regarding Audit Report No. 1113, Medical Benefits Plan: Claims Processing Audit

Ms. Joanna Munar presented the audit report. The City hired a third party, Wolcott & Associates Inc., to test medical and prescription drug benefit claims processed by Aetna, the Plan Administrator, during calendar years 2009 and 2010. Separately, City Auditor staff reviewed the City's benefit enrollment and change processes, which are critical to proper claims determinations. Enrollments and changes processed during fiscal years 2009/10 and 2010/11 were tested.

Wolcott concluded that Aetna processed medical plan claims with a high degree of accuracy, generally in line with industry standards. However, Wolcott identified areas

where claims processing and the City's summary plan description document can be improved. The auditors' tests found no errors in medical benefit enrollment and change processing, but concluded that certain controls can be improved to lessen the risk that errors will occur. The auditors concluded that terms of the administrative services agreement related to audit authority and performance guarantees can be improved.

Mr. Ken Nemec, Human Resources Benefits Manager was present. Councilwoman Milhaven asked him about the resolution with Aetna. Mr. Nemec agreed that the intention is to clarify the guidelines so there is less room for interpretation. Aetna has responded to the audit report, and the next step will be for City staff to meet with them.

Chair Klapp asked about the examples where participants had to pay more than they should have because Aetna felt the participant had to pay the co-pay no matter what. Mr. Nemec said this will be resolved with Aetna; plan members should be paying the lesser of the co-pay or the cost of the prescription. City Auditor Sharron Walker stated that in some instances Aetna was following its own standard practices where things were not spelled out in the City plan.

4. Discussion and possible direction to staff regarding Audit Report No. 1114, Cash Handling

Ms. Kyla Anderson presented the audit report. Since the City collects approximately \$75 million annually in cash and checks from 45 different locations, it is important to control cash handling practices. The auditors made unannounced visits to eight locations based upon their deposit volumes and audit history. They counted all cash on hand and reconciled it with transaction records. Additionally they reviewed each location's cash handling records and processes. It was found that overall City staff at the audited locations are appropriately accounting for and handling cash. However, the auditors recommend some improvements, including

- Strengthening controls at some locations
- Reducing some petty cash funds based on historical usage
- Ensuring the cash handling administrative regulation is followed in its entirety
- Updating the cash handling regulation to clarify the intended controls
- Using the City's centralized remittance processing function where possible

Ms. Anderson explained that since the audit report will be posted on the City's website, to protect City cash handling operations the report contains a summary of the audit results. Management in each of the areas audited has received a detailed memo of their department's audit and provided a response on their individual situations.

5. Discussion and possible direction to staff regarding Audit Report No. 1112, Selected Housing Programs - Section 8 and HOME

Ms. Joyce Gilbride presented the audit report. Community Services is responsible for administering the Section 8 and Home Investment Partnership (HOME) programs. Overall the auditors concluded that controls are in place to give reasonable assurance

that Section 8 and HOME procedures are followed. The two findings in the report relate to improvements that can be made to Section 8 program business practices that affect City monies.

HUD requires Section 8 funds to be kept in a separate bank account, which the City does. The City receives two deposits from HUD into this account on the first of each month. One is to cover housing and utility assistance payments; the other is an administrative fee the City receives for managing the Section 8 program. The average balance in this bank account is from \$1.5 million to \$2 million.

Checks for monthly housing and utility assistance payments are issued from the City's depository account, not the Section 8 account. Essentially this is a temporary loan to the Section 8 program by the City. Even though the funds are available, 30 to 40 days pass before the funds are reimbursed from the Section 8 account. The auditors noted there is no defensible reason for this kind of delay because the housing and utility assistance payment amounts have been documented, verified, and approved at the time the checks are issued from the City's bank account.

The administrative fee received by the City is intended to cover the cost of managing the Section 8 program. Any funds leftover at year end may be accumulated in a reserve fund for future years. The reserve is allowed to be spent for Section 8 administration or housing assistance. This reserve has grown to approximately \$500,000 over the past few years. The auditors found that even though these funds were available, some salaries and benefits for Section 8 staff had been paid out of the General Fund. For fiscal year 2009/10, the General Fund paid approximately \$238,000, and through May 2011, an additional \$165,000 has been spent. Ms. Gilbride noted that other City departments such as Accounting and the City Attorney's Office also support the Section 8 program. The administrative fee reserve could be used to offset some of those related support costs.

Mr. Bill Murphy, Executive Director of Community Services and Ms. Michelle Albanese, Community Services Manager, were in attendance.

Chair Klapp asked whether the plan is to draw checks on the Section 8 account, and if there is a reason the current practice is in place. Ms. Walker said this is apparently a historical practice that has been in place for some time that has never been reconsidered. The auditors have asked Community Services staff to work with Finance and Accounting to review and streamline their practices.

Councilwoman Milhaven inquired about recouping prior administrative expenses the City has borne. Ms. Gilbride said they would need to research what HUD would require. Accounting Director Mr. Jeff Nichols said that every year the City files a report with the federal government which includes details of expenditures related to each and every grant program. Staff could probably recoup what the City has spent this fiscal year; he was less certain about FY 2009/10. Chair Klapp said given the City's budget situation every little bit helps. She recognized that trying to recoup the funds for FY 2009/10 might not be practical, but she urged staff to at least try.

6. Discussion and possible direction to staff regarding Report No. 1116 FY 2010/11 Report on Audit Follow-Ups

Ms. Walker noted that the results are similar to the corresponding quarter last year. Attachment D to the report summarizes the savings that audits have identified over the last five years. This year staff has done a great job of identifying savings and revenue enhancements. She wanted to acknowledge their efforts for the Audit Committee.

Councilwoman Milhaven asked whether any of the items that have not been implemented represent any significant risk. Ms. Walker said that Attachment C breaks out the recommendations that were not implemented. There are good reasons why a different approach has been adopted in most cases. She added that under tangible property asset management, she is not sure that the best choice was made regarding retaining tags of assets which are disposed of. The department has changed to tags that shred as they are removed. However she does not see this as a serious concern at this time because it is standard practice for auditors to look at previous audits of a department. This issue would be reconsidered during the next related audit.

Chair Klapp suggested eliminating the items which have been on the list for a number of years. Ms. Walker said she keeps five rolling years of data, so next year most of these items, which are old, will be gone from the report.

Chair Klapp said it appears that City departments cooperate well with the auditors. Ms. Walker said she believes the good implementation rate occurring now is because the Audit Committee wanted the audit follow-up program. Councilwoman Milhaven congratulated her on implementing the follow-up program effectively.

7. Discussion and possible direction to staff regarding draft Ordinance 3942, authorizing access to executive session minutes and incorporating new public records law exemption

Ms. Walker noted that this item is on the upcoming City Council meeting agenda, and she wanted the Audit Committee to have the opportunity to preview it. The first part of the proposed ordinance would allow the City Auditor to have access to executive session meeting minutes of City Council and City boards and commissions. It is City Council's decision of whether to make this change. The second part of the proposed ordinance is simply updating City Code for the change in state law to exempt city auditors' work from public records. Her background with the State Auditor General's office led her to request these law changes, which will put them on a par with county and state auditors and make their job easier.

8. Discussion and Possible Direction to Staff regarding status of FY 2011/11 Audit Plan

Ms. Walker stated that the auditors have accomplished the number of audits they planned to. The only change from the original plan was that they added the residential solid waste analysis, which pushed back the meter reading audit. She noted that this is

the first time that the City Auditor's Office has completed one hundred percent of the audit plan. Staff has been doing a terrific job keeping up with the volume of work.

9. Discussion of Agenda Items for Next Audit Committee Meeting on August 22, 2011

Ms. Walker noted that the next meeting will cover the meter reading audit. One item from the FY 2011/12 audit plan, the SkySong ground lease, may be ready. She told the Committee Members to let her know if they would like to have any other items added to the agenda.

Public Comment

No members of the public wished to address the Committee.

Adjournment

The meeting adjourned at approximately 4:31 p.m.

Respectfully submitted,
A/V Tronics, Inc. DBA AVTranz.